

Report
of the
Examination of
Calumet Equity Mutual Insurance Company
New Holstein, Wisconsin
As of December 31, 2002

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Jorge Gomez, Commissioner

Wisconsin.gov

July 16, 2003

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Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
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Commissioner:

In accordance with your instructions, an examination has been performed as of
December 31, 2002, of the affairs and financial condition of

CALUMET EQUITY MUTUAL INSURANCE COMPANY
NEW HOLSTEIN, WISCONSIN

and the following report is respectfully submitted:

I. INTRODUCTION

The last examination of this company was made in 1998 as of December 31, 1997.

The current examination covered the intervening time period ending December 31, 2002, and included a review of such subsequent transactions deemed essential to complete this examination.

The Summary of Examination Results contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on March 10, 1873, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Mutual Fire Insurance Company of the Town of New Holstein. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were two amendments to the articles of incorporation and no amendments to the bylaws. In 1998, the authorized territory of the company

was expanded to include 16 counties. In the same year, the number of directors was changed from eight to seven members.

A review of the certificate of authority revealed that the company is currently licensed to write business in the following counties:

Brown, Calumet, Dodge, Fond du Lac, Green Lake, Kewaunee, Manitowoc, Oconto, Outagamie, Ozaukee, Shawano, Sheboygan, Washington, Waupaca, Waushara, and Winnebago

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance.

A review was made of the policy and application forms currently used by the company. The company issues an approved policy with or without endorsements for terms of one year with premiums payable on the advance premium basis. Policy fees charged to policyholders are retained by the company.

Business of the company is acquired through 193 agents, none of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
Dwelling Fire and EC	17%
Homeowner and Mobile homeowner	17%
Standard Farm	15%
Standard Non-Farm	15%
Farmowner	15%
Commercial	15%

Agents do not have authority to adjust losses. The majority of losses are adjusted by the company's loss inspector. The loss inspector is a salaried employee who receives \$.36 per mile for travel allowance. Directors may also adjust losses. They are paid between \$15 to \$120 per claim depending on the size of the claim, plus the above travel allowance. The adjustor has the authority to settle claims up to \$25,000. Losses in excess of this amount are reviewed by the loss adjustment committee.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of seven members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Jerry Criter	Farmer	Chilton	2004
Gerald Heus	Excavation Contractor	Chilton	2004
James Whittaker	Manager	Chilton	2005
Paul Hofacker	Farmer	Appleton	2005
Carl Holzcshuh	Farrier	Menasha	2006
James Scholz	Retired	Chilton	2006

Effective April 1, 2003, a member of the board resigned. The board is currently recruiting a new director for the interim to the next annual meeting. Members of the board currently receive \$100 for each meeting attended and \$.36 for travel expenses. Board members who are also officers do not receive a per diem for attending meetings.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified.

Officers serving at the present time are as follows:

Name	Office	2003 Salary
Jerry Criter	President	\$12,000
Gerald Heus	Vice President	4,000
James Whittaker	Secretary/Treasurer	48,600

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Executive Committee

Jerry Criter – President

Gerald Heus – Vice President

James Whittaker – Secretary/Treasurer

Adjusting Committee

Consists of any one member of the Executive Committee and the adjuster(s) of the loss.

Rate Committee

Consists of the Executive Committee and any other board member called to assist.

Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Net Losses and LAE Incurred	Policies In-Force	Net Income	Admitted Assets	Policyholders Surplus
2002	\$740,525	\$912,427	2,743	\$(547,940)	\$1,559,863	\$ 463,777
2001	714,191	756,914	2,462	(339,729)	2,047,339	1,172,569
2000	770,287	814,787	2,360	(352,887)	2,306,561	1,568,827
1999	990,112	506,962	2,590	118,092	2,719,905	1,827,686
1998	931,247	856,428	3,026	(236,118)	2,558,662	1,667,626

The ratios of premiums written, gross and net, to surplus as regards policyholders during the past five years were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Gross	Ratios Net
2002	\$1,507,507	\$871,221	\$ 463,777	325%	188%
2001	1,261,678	756,226	1,172,569	107	64
2000	1,172,594	693,481	1,568,827	74	44
1999	1,365,617	972,153	1,827,686	74	53
1998	1,383,895	946,973	1,677,626	82	56

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Composite Ratio
2002	\$912,427	\$461,264	\$740,525	123%	53%	176%
2001	756,914	408,646	714,191	106	54	160
2000	814,787	391,242	770,287	106	56	162
1999	506,962	435,083	990,112	51	45	96
1998	856,428	429,564	931,247	92	45	137

The company has had both underwriting and net losses in four of the past five years. Losses have been extensive in the past three years due to area storms and the company's localized market. That, combined with a higher than industry average expense ratio, has given the company a composite ratio near or above 150% in four of the past five years. Net earned premiums decreased between 1999 and 2001, but showed a slight increase in 2002 with 281 new policies in force. At the same time, net losses increased for a surplus decrease of 72% during the

period under examination, with a 70.8% decrease in the past year. The company has taken steps in the current year to improve its financial condition including placing a moratorium on new business, reinspecting renewal business, increasing policy fees, reducing commissions, changing the reinsurance program to reduce risk, and lowering per diems for directors.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2003
Termination provisions:	Either the Company or the Reinsurer may terminate this Contract of Reinsurance and/or any of the attached exhibits as of 12:01 A.M. Central Standard Time, January 1, 2004, or any subsequent January 1, by giving to the other party at least 90 days advance notice in writing.

The coverages provided under this treaty are summarized as follows:

- | | |
|----------------------|--|
| Type of contract: | Class A - Excess of Loss Reinsurance |
| Lines reinsured: | All business classified as Casualty business |
| Company's retention: | \$1,500 in respect to each and every loss occurrence |
| Coverage: | 100% of each and every loss occurring on the business covered by this contract, including loss adjustment expenses, except that the company bears sole responsibility for milk contamination losses. Coverage is subject to maximum policy limits of \$1,000,000 per occurrence, in any combination of bodily injury and property damage liability, \$5,000 for medical payments, per person: \$25,000 per accident. |
| Reinsurance premium: | 57.5% of the premium written for each and every policy. Minimum retention of \$140,000. |
- | | |
|----------------------|---|
| Type of contract: | Class B First Surplus Reinsurance |
| Lines reinsured: | All property business written by the company |
| Company's retention: | \$350,000 per ceded risk, plus at least 50% on a pro rata basis per ceded risk when the company's net retention is \$350,000 or less in respect to a risk. In any case the company shall retain an annual aggregate deductible equal to 10% of the loss and loss adjustment expenses otherwise recoverable. |
| Coverage: | Up to \$800,000 on a pro rata basis when the company's net retention is \$350,000 or more in respect to a risk. When the company's net retention is \$350,000 or less in respect to a risk, the company may cede on a pro rata basis up to 50% of such risk. |

Reinsurance Premium:	100% of the unearned premium applicable to property business. Pro rata share of all premiums and fees charged by company corresponding to the amount of each risk ceded.
Ceding Commission:	15% to 35%, depending on loss experience
3. Type of contract:	Class C-1 Excess of Loss - First Layer (Formula Rated)
Lines reinsured:	All property business written by the company
Company's retention:	\$40,000 per occurrence \$30,000 annual aggregate deductible
Coverage:	100% of any loss, including loss adjustment expense, in excess of \$40,000, subject to a limit of liability to the reinsurer of \$60,000.
Reinsurance Premium:	Based on experience over the past four years with load factor of 125%. Minimum rate: 5% of current net premiums written Maximum rate: 22% of current net premiums written Current rate is 15% Premium deposit: \$159,000; Minimum premium of \$128,000.
4. Type of contract:	Class C-2 Excess of Loss - Second Layer (Flat rated)
Lines reinsured:	All property business written by the company
Company's retention:	\$100,000
Coverage:	100% of any loss, including loss adjustment expense, in excess of \$100,000, subject to a limit of liability to the reinsurer of \$100,000
Reinsurance premium:	1.75% of the company's current net premiums written in respect to the business covered Premium deposit: \$18,000; Minimum premium of \$15,000
5. Type of contract:	Class C-3 – Third Excess of Loss
Lines reinsured:	Property
Company's retention:	\$200,000
Coverage:	100% of each loss occurrence, excluding LAE, in excess of \$200,000 up to a maximum \$150,000.
Reinsurance premium:	1.25% of net premiums written with a deposit premium of \$13,200 payable in monthly installments. Minimum premium of \$11,000
6. Type of contract:	Class D/E Stop Loss Reinsurance
Lines reinsured:	All business written by the company
Company's Retention:	60% of net written premium

Coverage:	100% of the amount, if any, by which the aggregate of the company's losses, including loss adjustment expenses exceed the retention. Minimum retention of \$525,000
Reinsurance premium:	<p>Current rate based on a formula calculation which takes into account the losses incurred by the reinsurer under this contract for the last eight years</p> <p>Minimum rate: 6% of the current net written premiums</p> <p>Maximum rate: 25% of the current net written premiums</p> <p>The rate for the current annual period is 15%.</p> <p>Deposit premium \$162,000; minimum premium \$130,000</p>

III. FINANCIAL DATA

The following financial statements were filed with the Commissioner of Insurance in the company's annual statement as of December 31, 2002. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Calumet Equity Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2002

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in Company's Office	\$ 60	\$	\$	\$ 60
Cash Deposited in Checking Account	8,649			8,649
Cash Deposited at Interest	463,295			463,295
Bonds (at Amortized Cost)	81,953			81,953
Stocks or Mutual Fund Investments (at Market)	695,740			695,740
Real Estate	65,451			65,451
Premiums and Agents' Balances and Installments:				
In Course of Collection	3,888			3,888
Deferred and Not Yet Due	230,850			230,850
Investment Income Accrued		9,255		9,255
Electronic Data Processing Equipment	722			722
Furniture and Fixtures	<u>977</u>	<u> </u>	<u>977</u>	<u> </u>
TOTALS	<u>\$1,551,585</u>	<u>\$9,255</u>	<u>\$977</u>	<u>\$1,559,863</u>

Calumet Equity Mutual Insurance Company
Statement of Assets and Liabilities (cont.)
As of December 31, 2002

Liabilities and Surplus

Net Unpaid Losses	\$116,030
Unpaid Loss Adjustment Expenses	6,800
Commissions Payable	57,857
Fire Department Dues Payable	2,071
Unearned Premiums	755,391
Reinsurance Payable	98,992
Payroll Taxes Payable (Employer's Portion)	5,187
Other Liabilities:	
Expense Related:	
Accounts Payable	16,207
Accrued Property Tax	3,304
Nonexpense Related:	
Premiums Received in Advance	<u>34,247</u>
TOTAL LIABILITIES	1,096,086
Policyholders' Surplus	<u>463,777</u>
TOTAL	<u><u>\$1,559,863</u></u>

Calumet Equity Mutual Insurance Company
Statement of Operations
For the Year 2002

Net Premiums and Assessments Earned		\$ 740,525
Deduct:		
Net Losses Incurred	\$809,671	
Net Loss Adjustment Expenses Incurred	102,756	
Other Underwriting Expenses Incurred	<u>461,264</u>	
Total Losses and Expenses Incurred		<u>1,373,691</u>
Net Underwriting Gain (Loss)		(633,166)
Net Investment Income:		
Net Investment Income Earned	2,273	
Net Realized Capital Gains	<u>6,796</u>	
Total Investment Income		<u>9,069</u>
Other Income:		
Miscellaneous	24	
Installment and Policy Fees	<u>76,133</u>	
Total Other Income		<u>76,157</u>
Net Income (Loss) Before Policyholder Dividends and Before Federal Income Taxes		<u>(547,940)</u>
Net Income (Loss) Before Federal Income Taxes		<u>(547,940)</u>
Net Income (Loss)		<u>\$ (547,940)</u>

Calumet Equity Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2002

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2002	2001	2000	1999	1998
Surplus, beginning of year	\$1,172,569	\$1,568,827	\$1,827,686	\$1,677,626	\$1,813,162
Net income	(547,940)	(339,729)	(352,887)	118,092	(236,118)
Net unrealized capital gains or (losses)	(161,741)	(57,488)	92,978	29,881	99,387
Change in non-admitted assets	889	955	1,050	2,087	1,195
Change in surplus notes					
Other gains and (losses) in surplus:					
Rounding		4			
Surplus, end of year	<u>\$ 463,777</u>	<u>\$1,172,569</u>	<u>\$1,568,827</u>	<u>\$1,827,686</u>	<u>\$1,677,626</u>

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders' surplus. The amount reported by the company as of December 31, 2002, is accepted.

Reclassification Account	Debit	Credit
Payroll Taxes Payable	\$2,540	\$
Amounts Withheld for the Account of Others	_____	<u>2,540</u>
Total	<u>\$2,540</u>	<u>\$2,540</u>

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Loss Adjusting—It is recommended that the company's loss adjustment committee consist of at least three directors in accordance with s. 612.13 (4), Wis. Stat.

Action— Noncompliance – See comments in the Current Examination Results section of this report under the caption "Claims Adjusting."

2. Invested Assets—It is recommended that the company execute a safekeeping agreement for all securities held in safekeeping in accordance with s. 610.23, Wis. Stat., and the NAIC Examiners Handbook.

Action—Compliance

3. Transition into the New Investment Rule—It is recommended that the company eliminate any Type 1 investment deficiency and become compliant with s. Ins 6.20, Wis. Adm. Code, by December 31, 1999.

Action—Compliance

4. Premiums and Agents' Balances in Course of Collection—It is recommended that the company reconcile its accounts receivable adjusted balance with the general ledger.

Action—Compliance

5. Electronic Data Processing Equipment—It is recommended that the company retain a detailed schedule of all depreciable assets in accordance with s. Ins 6.80 (4), Wis. Adm. Code.

Action—Compliance

6. Unpaid Loss Adjustment Expenses—It is recommended that future annual statements make a more reasonable estimate for unpaid loss adjustment expenses which include unallocated loss adjustment expenses.

Action—Compliance

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with two apparent conflicts being noted. One of the directors disclosed he is also a director and the treasurer of Wisconsin Reinsurance Corporation, while a second director disclosed he is also a crop appraiser for Rural Community Insurance Company. There did not appear to be any voting issues noted in the minutes upon which either director needed to abstain.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity Bond	\$ 500,000
Worker's Compensation:	Statutory
Employer's Liability:	
Each Accident	1,000,000 each accident
Each Employee	1,000,000 policy limit
Policy Limit	1,000,000 each employee
Commercial Umbrella:	
Aggregate Limit	3,000,000
Products/Completed Operation	2,000,000
Personal and Advertising Injury Limit	1,000,000
Limit Per Occurrence	1,000,000
Disease-Each Employee	1,000,000
Retained Limit	10,000
Commercial Liability Rental	
Aggregate Limit	3,000,000
Personal and Advertising Injury Limit	1,000,000
Limit per Occurrence	1,00,000
Fire Damage Limit	100,000 any one fire
Medical Expense Limit	5,000 any one person
Building	175,000
Liability and Medical Expense	1,000,000
Fire Legal Liability	100,000
Professional Liability	
Company Professional Liability	3,000,000
Directors and Officers Liability	3,000,000
Deductible per Claim	10,000
Employment Practices Liability	1,000,000
Deductible per Claim	5,000

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. A sampling of new applications and of renewal business is inspected by the inspector/adjuster, a salaried employee.

Claims Adjusting

The company has an adjusting committee whose function is to adjust and supervise the adjustment of losses. All losses above \$25,000 are subject to the approval of the committee.

The prior examination noted the loss adjusting committee did not consist of at least three directors as required by s. 612.13 (4), Wis. Stat. The company complied the following year by naming the executive committee, which consists of the president, vice-president and secretary/treasurer, and the adjustor(s) of the loss as the adjusting committee. However, a review of the company's minutes noted for the two prior years the loss adjustment committee has consisted of any one member of the executive committee and the adjuster(s) of the loss. It is again recommended that the company's loss adjustment committee consist of at least three directors in accordance with s. 612.13 (4), Wis. Stat.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2002.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's Electronic Data Processing environment. Access to the computers is limited to people authorized to use the computers. Company personnel back up the computers daily and the backed-up data is kept off-site.

A manual which describes how to use the company's software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Disaster Recovery Plan

A disaster recovery plan identifies steps to be performed in case the company loses a key employee, is not able to access its computer, information on its computer was lost, or the office building was destroyed, to name a few contingencies. The company has developed a disaster recovery plan. The company's disaster recovery plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

- (1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and
- (2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutuals allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3 in the following table.

1. Liabilities plus \$300,000	\$1,396,086
2. Liabilities plus 33% of gross premiums written	1,593,563
3. Liabilities plus 50% of net premiums written	1,531,697
4. Amount required (greater of 1, 2, or 3)	1,593,563
5. Amount of Type 1 investments as of 12/31/2002	<u>672,876</u>
6. Excess or (deficiency)	<u>\$ (920,687)</u>

The company does not have sufficient Type 1 investments.

A recommendation was made in the prior examination that the company eliminate any Type 1 investment deficiency and become compliant with s. Ins 6.20, Wis. Adm. Code, by December 31, 1999. The company did come into compliance with that recommendation. However, the company has been Type 1 deficient in all subsequent years.

The company received permission to hold 30% of admitted assets in Type 2 investments. At year end the company held 37% of admitted assets in these investments, mainly due to the reduction in admitted assets. It is recommended that the company either comply with the existing limitation of investing no more than 30% of admitted assets in Type 2 investments, or request a modification to the limitation of OCI with the proper justification for such request.

ASSETS

Cash and Invested Cash

\$472,004

The above asset is comprised of the following types of cash items:

Cash in company's office	\$ 60
Cash deposited in banks-checking accounts	8,649
Cash deposited in banks at interest	<u>463,295</u>
Total	<u>\$474,004</u>

Cash in the company's office at year-end represents the company's petty cash fund.

A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of four accounts maintained in two banks. Verification of checking account balances was made by obtaining confirmations directly from the depositories and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of sixteen deposits in ten depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2002 totaled \$26,354 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 1.3% to 7.3%. Accrued interest on cash deposits totaled \$7,522 at year-end.

Book Value of Bonds

\$81,953

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2002. Bonds owned by the company are located in a safety deposit box in a local bank or held under a custodial agreement.

Bonds held in the safety deposit box were physically inspected by the examiners. Bonds held under the custodial agreement were verified through direct confirmation from the custodian and the year-end trust statement. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds

was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2002 on bonds amounted to \$9,233 and was traced to cash receipts records. Accrued interest of \$1,641 at December 31, 2002, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments

\$695,740

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2002. Stocks owned by the company are located in a safety deposit box at a local bank.

Stock certificates were physically examined by the examiners. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. However, the aggregate investment in common stocks, preferred stocks, and mutual funds exceeds the 30% of admitted assets approved by this office. The majority of this investment is in Wisconsin Reinsurance and NAMICO stock at \$434,634. The company has not purchased Type 2 investments during the period under examination, but the 39% reduction in admitted assets since the prior examination has increased the company's Type 1 investment deficiency. A recommendation regarding this issue was made in the section of this report titled Investment Rule Compliance.

Dividends received during 2002 on stocks and mutual funds amounted to \$12,700 and were traced to cash receipts records. Accrued dividends of \$92 at December 31, 2002, were checked and allowed as a nonledger asset.

Book Value of Real Estate

\$65,451

The above amount represents the company's investment in real estate as of December 31, 2002. The company's real estate holdings consisted of the company's home office building valued at \$9,308 and a rental property valued at \$56,143. The company is permitted to hold the rental property due to prior approval from this office.

The required documents supporting the validity of this investment were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

Agents' Balances or Uncollected Premiums **\$3,888**

The above ledger asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of individual agent's accounts verified the accuracy of this asset.

Premium and Installments Booked but Deferred and Not Yet Due **\$230,850**

The above ledger asset represents premiums and agents' balances which are receivable, but not yet due because the insureds have chosen other than an annual billing mode. This asset was documented by an automated report, itemizing the company's calculation of installments booked but deferred and not yet due for each policy in force as of December 31, 2002. A review of individual policy information and subsequent receipt for policies selected on a sample basis verified the accuracy of this asset.

Investment Income Due and Accrued **\$9,255**

Interest due and accrued on the various assets of the company at December 31, 2002, consists of the following:

Cash Deposited at Interest	\$7,522
Bonds	1,641
Stocks & Mutual Funds	<u>92</u>
Total	<u>\$9,255</u>

The examiner verified this amount by recalculating and tracing amounts to subsequent receipts.

Equipment, Furniture, and Supplies**\$977**

This asset consists of \$977 of furniture and fixtures owned by the company at December 31, 2002. In accordance with annual statement requirements, this amount has been deducted as an asset not admitted.

Electronic Data Processing Equipment**\$722**

The above amount represents the company's investment in electronic data processing equipment at December 31, 2002. The amount is reported net of accumulated depreciation and excludes software. Electronic data processing equipment is calculated using the straight-line method. This asset was verified by reviewing purchase information and recalculating accumulated depreciation.

LIABILITIES AND SURPLUS

Net Unpaid Losses

\$116,030

This liability represents losses incurred on or prior to December 31, 2002, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule. Differences are reflected in the section of this report captioned "Reconciliation of Policyholders' Surplus."

	Company Estimate	Examiners' Development	Difference
Incurred But Unpaid Losses	\$538,764	\$525,126	\$13,638
Less:			
Reinsurance Recoverable on Unpaid Losses	<u>422,734</u>	<u>409,096</u>	<u>13,638</u>
Net Unpaid Losses	<u>\$116,030</u>	<u>\$116,030</u>	<u>\$ 0</u>

The examiners developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2002. To the actual paid loss figures was added an estimated amount for those 2002 and prior losses remaining unpaid at the examination date. The examiner's actual development of unpaid losses indicated a favorable development as compared to the company's estimate. Although the company hit its stop loss for 2002, the possibility for some adverse development remains, so no adjustment will be made for positive development.

While reserves for unpaid losses were sufficient, no estimate for IBNR nonproperty losses was included on the annual statement. The company retains \$1,500 on each nonproperty loss. Although IBNR nonproperty losses reported for 2002 would be covered by the stop loss recovery, there were other IBNR losses noted for nonproperty for the period under examination. No IBNR reserve for nonproperty losses was noted for any of those years. It is recommended that the company include an IBNR estimate for nonproperty losses for both the gross and recoverable amounts when completing Schedule J-1 of the annual statement.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made

promptly and in accordance with policy provisions upon the submission of a proper proof of loss.

In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

Unpaid Loss Adjustment Expenses **\$6,800**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2002, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is based on the number of open claims at year end and the related adjusting expenses.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Unearned Premiums **\$755,391**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology.

Reinsurance Payable **\$98,992**

This liability consists of amounts due to the company's reinsurer at December 31, 2002, relating to transactions which occurred on or prior to that date.

Class A Liability Premium	\$23,185
Class C-1 Premium	21,425
Class C-2 Premium	(575)
Class C-3 Premium	2,475
Class D/E Premium	38,300
First Surplus Premium	16,684
First Surplus Commission	<u>(2,502)</u>
Total Due	<u>\$98,992</u>

Subsequent cash disbursements and reinsurance accountings verified the amount of this liability.

Fire Department Dues Payable **\$2,071**

This liability represents the fire department dues payable at December 31, 2002. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Commissions Payable **\$57,857**

This liability represents the commissions due to agents on premium which has been received as well as premium which has been booked but deferred and not yet due. The examiners reviewed the company's commission calculation and found the liability to be correctly calculated. The balance was verified to subsequent cash disbursements.

Amounts Withheld for the Account of Others **\$2,540**

This liability represents employee payroll deductions in the possession of the company at December 31, 2002. Supporting records and subsequent cash disbursements verified this item. The balance for this account was included in payroll taxes payable on the annual statement. A reclassification was made reducing payroll taxes payable by \$2,540 and reporting that amount in this account. It is recommended that amounts withheld for the account of others be reported on the correct line on the annual statement according to Town Mutual Annual Statement Instructions.

Payroll Taxes Payable **\$2,647**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2002, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item. However, the company included amounts withheld for the account of other in this balance. A reclassification was made reducing the reported balance of \$5,187 by \$2,540 to the current balance. A recommendation regarding this account was made in Amounts Withheld for the Account of Others.

Accounts Payable **\$16,207**

This account represents various expenses the company incurred prior to December 31, 2002, which had not yet been paid. The balance includes accrued salaries, vacation, and sick pay, as well as miscellaneous office bills. The examiner's review of supporting

records and subsequent cash disbursements, in conjunction with a search for unrecorded liabilities, determined this balance to be adequately stated.

Accrued Property Taxes

\$3,304

This liability represents unpaid property taxes as of December 31, 2002. A review of company records and subsequent cash disbursements verified this liability.

Premiums Received in Advance

\$34,247

This liability consists of premiums due in 2003, which were received as of December 31, 2002. The examiner traced the balance to a detail report of advance premium, and verified a sample by review of policy files and cash receipt records.

V. CONCLUSION

Calumet Equity Mutual Insurance Company is a town mutual insurer with an authorized territory of sixteen counties. The company has been in business for 130 years providing property and liability insurance to its policyholders.

At December 31, 2002, the company reported admitted assets of \$1,559,863, liabilities of \$1,096,086, and surplus of \$463,777. The company has experienced extensive losses in four of the five years under examination, and has reported both underwriting and net losses during those years. There has been a 72% loss to surplus since the prior examination, and 2002 surplus declined 70% from 2001 surplus. The company has taken steps subsequent to year-end to improve its financial condition, including placing a moratorium on new business, reinspecting renewal business, changing the reinsurance program to reduce risk, increasing policy fees and reducing commissions and per diems for directors.

The examination determined that the company complied with five of its prior six examination recommendations. Four recommendations were made in the current examination, one of which was repeated from the prior examination. The recommendations are listed in summary form on the following page.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 19 - Claims Adjusting—It is again recommended that the company's loss adjustment committee consist of at least three directors in accordance with s. 612.13 (4), Wis. Stat.
2. Page 21 - Investment Rule Compliance—It is recommended that the company either comply with the existing limitation of investing no more than 30% of admitted assets in Type 2 investments, or request a modification to the limitation of OCI with the proper justification for such request.
3. Page 26 - Net Unpaid Losses—It is recommended that the company include an IBNR estimate for nonproperty losses for both the gross and recoverable amounts when completing J-1 of the annual statement.
4. Page 28 - Amounts Withheld for the Account of Others—It is recommended that amounts withheld for the account of others be reported on the correct line on the annual statement according to Town Mutual Annual Statement Instructions.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Mark Knievel of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Respectfully submitted,

Jean Suchomel
Examiner-in-Charge